Oil and Gas Development Company Limited

Conference Call on Half Year Financial Results FY 2019 (July 2018 – December 2018)

Presenters: **Mr. Zahid Mir (Managing Director / CEO)**
Mr. Irteza Ali Qureshi (Chief Financial Officer)
Dr. Muhammad Saeed Khan Jadoon (Executive Director, Exploration)
Dr. Naseem Ahmad (Executive Director, Production)

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Time: **5:00 PM (Pakistan Standard Time)**

Mr. Zahid Mir: Good afternoon and welcome to OGDCL's Half Year FY2019 Financial Results Conference Call. My name is Zahid Mir, I am MD/CEO of OGDCL. Before proceeding with the presentation, let me first introduce my team to you. I've with me here Mr. Irteza Ali Qureshi, Chief Financial Officer, Dr. Muhammad Saeed Khan Jadoon, Executive Director (Exploration) and Dr. Naseem Ahmad, Executive Director (Production).

Mr. Zahid Mir: I understand that our Investor Relations team has already sent you a presentation on OGDCL's Half Year Results 2018-19. Let's begin with page 2 of the presentation where I'll ask you to go over the legal disclaimer first. I will take a short pause while you read the legal disclaimer.

Ladies & gents, I am pleased to report OGDCL's operational & financial performance during the financial year 2018-19. OGDCL, being the largest upstream player in Pakistan, enjoys the largest share of exploration acreage in the country, which stands at 26% of the total awarded acreage. As of June 2018, OGDCL held 55% of the country's recoverable oil reserves and 32% of the country's recoverable gas reserves. In terms of production, currently, OGDCL delivers 29% of Pakistan's gas output and 47% of its oil output. Our remaining 2P recoverable reserves estimates, as at December 31, 2018, stood at an impressive 917 MMBOE. OGDCL have a portfolio of 106 Development & Production Leases (D&PLs) out of which 69 D&PLS are 100% owned and operated while 37 are non-operated D&PLs where we act as non-operators having Joint Venture agreements with foreign as well as local E&P companies. OGDCL operations are spread out all over Pakistan. During the fiscal year from July 2018 to December 2018, OGDCL reported average daily net crude oil, gas and LPG production of 40,846 barrels, 990 MMcf and 798 Metric tons. During the period under review, OGDCL spud six wells including three exploratory/appraisal wells and three development wells. I am pleased to report that during the 6 months period, OGDCL also made two discoveries.

Moving on to slide 4, you can see a map which clearly shows OGDCL's dominant position in all the prospective areas of Pakistan. OGDCL holds a diverse portfolio of exploratory assets currently constituting forty-six owned and operated joint venture exploration licenses along with holding working interest in five blocks operated by other exploration and production companies. These exploratory licenses are spread across all four provinces of the Country covering an area of 82,835 sq. kms as at 31st December 2018 representing the largest exploration acreage held by any E&P Company in Pakistan.

To carry on with the presentation, I will now ask Mr. Irteza Ali Qureshi, Chief Financial Officer, and other heads of departments to take you through the next few slides of this presentation.

Mr. Irteza Ali Qureshi: Ladies and gentlemen, this is Irteza Qureshi, I am the Chief Financial Officer in OGDCL.

Turn to slide # 5, on the financial front, OGDCL continues to deliver robust financial results for the half year ended 31 December 2018 as its Sales Revenue and Profit before Tax climbed to Rs 126.898 billion and Rs 84.739 billion, showing growth of 32% and 63%, respectively. These financials are primarily supported by higher average realized price of crude oil @ US$ 62.22/barrel against US$ 48.69/barrel in the relative period last year. In addition to the above, OGDCL recorded increase in the realized price for gas and LPG averaging Rs 317.33/Mcf and Rs 69,295/ton compared with Rs 253.83/Mcf and Rs 53,591/ton, respectively in the comparable period. Operating profit margin and net profit margin were 56% & 45%, respectively with EPS of Rs 13.20. In addition, the Directors of the Company today approved a second interim payable cash dividend of Rs 3 per share for the year.

I now hand over the presentation to Dr. Muhammad Saeed Khan Jadoon who is OGDCL's Head of Exploration to continue with this presentation.

Dr. Muhammad Saeed Khan Jadoon: This is Dr. Saeed Jadoon and I will be taking you through slide # 6. Being the market leader in E&P sector of Pakistan, OGDCL possesses the largest exploration acreage, which as of 31 December 2018 stood at 82,835 sq. kms, representing 26% of the Country's total area under exploration. In line with its exploration-led growth strategy to replenish reserves and enhance production, OGDCL during the period under review acquired 584 line kms of 2D and 394 sq. kms of 3D seismic data. The 2D and 3D seismic data acquisition represents 50% and 52% of total seismic data acquired in the Country during the current period under review. Moreover, 4,109 line kms of 2D seismic data has been processed/reprocessed by utilizing in-house resources.

In addition to the above, OGDCL during the reporting period spud six wells, comprising of three exploratory wells namely Siab-1, Qadirpur Deep X-1 and Garhi X-2 and three development wells namely Qadirpur-60, Pasakhi NE-2 and Chanda-5. OGDCL's exploratory efforts to locate new hydrocarbon reserves during the period under review yielded two oil and gas discoveries namely Chanda-1 and Mela-5 in district Kohat, KPK province. I will now hand over the presentation to Dr. Naseem Ahmad, who is Executive Director of Production.

Dr. Naseem Ahmad: Hello everyone, this is Naseem Ahmad, Executive Director of Production. The Company during six months period contributed around 46% and 29% of the Country's total oil and natural gas production, respectively. Moreover, seven new operated wells were injected in the production gathering system which cumulatively yielded gross crude oil and gas production of 116,417 barrels and 2,251 MMcf, respectively.

During the period under review, OGDCL, on gross basis, produced 19.40 MMBOEs showing an increase of 2% when compared with the same period last year. Despite natural decline and short lifting of crude oil by refineries at Kunnar, KPD-TAY, Nashpa and TOC fields owing to pile-up of furnace oil stock, Company's average net saleable crude oil production remained stable at 40,846 barrels per day owing to increase in production from Pasakhi, Chanda, Mela and Non-operated JV fields coupled with start-up of production at Chutto-1. However, average net saleable gas production in comparison to the corresponding period last year is slightly lower by 2% primarily on account of natural decline and less gas intake by UPL-I due to extended ATA of UPL-I, which started from 16 October 2018 to 8 December 2018. Moreover, tripping of turbines at LPL, Engro Power and FKPCL along with decline in Non-Operated JV production impacted gas output. Regarding LPG production, OGDCL witnessed 24% surge mainly due to production commencement from Nashpa field in conjunction with increase in production from Sinjhoro and KPD fields.

Going over to slide 8, where latest status on our various development projects is mentioned.

For Dhok Hussain development project, the early production facilities have been installed comprising of separation and dehydration facilities. SNGPL sales gas pipeline completion is awaited after which gas will be injected into SNGPL network. Bitrisim Development includes Bitrism West 1, Bitrism West 2, Gundanwari and Chabaro wells. Bitrism West 1 & Bitrism West 2 will be put on production by May 2019 by utilizing available capacity at Sinjhoro Plant. Subsequently, after completion of Bitrism Project facilities processing of Gundanwari & Chabaro will also be started. Mela project's scope includes Mela facilities upgradation and laying of Mela-Nashpa gas pipeline. Thal West & Thal East gas will be processed at Kandanwari Plant where laying of flow lines has commenced. OGDCL is looking for a gas buyer to sign a GSA for sale of Jhal Magsi Gas. Project development activities of Jhal Magsi will be started accordingly. Khewari Development includes production hook-up of Suleman 1, Suleman 2 and Mithri Wells. The wells have approximately 15% CO_2 content. Gas processing facilities will be installed for removal of CO_2 and gas will be supplied to SSGCL's network.

Now I ask Mr. Irteza Ali Qureshi, CFO, to continue with this presentation.

Mr. Irteza Ali Qureshi: Thank you. Looking at slide number 9, which shows a graphical illustration of our financial performance. Increase in net sales revenue by 32% was due to increase in oil, gas and LPG prices, as well as some increase in LPG production. Further, there is a gain on account of exchange rate devaluation which is approximately 19.8% of the total increase in the revenues. Operating expenses have gone up by 5%, owing largely to PKR 1.3 billion increase in depreciation and amortisation, as well as PKR 0.5 billion increase in the work-over charges for the current fiscal year as 11 work-overs wells against 6 workovers in the corresponding period last year. Profit after tax increased by 55%, mainly due to increase in sales revenues as well as controlled costs. Decrease in exploration and prospecting expenditure of 39% was largely because only one well, Wasan-1, was declared as a dry well during the current period as opposed to three wells in the corresponding period of previous year.

Turning to slide number 10, which shows key performance indicators of the Company.

To take the presentation to conclusion, I now hand over the presentation back to our MD/CEO.

Mr. Zahid Mir: Thank you Irteza. OGDCL remains steadfast in its resolve to carry out vigorous exploratory endeavours, expedite completion of ongoing development projects and exercise financial discipline while undertaking new development activities to maintain and improve business operational performance alongside creating material value for the shareholders in the years to come.

Ladies and gentlemen, this concludes our presentation for today and I thank you all for joining in the conference call. We now ask the operator to conduct a Q&A session, which we expect to be not more than 20 minutes duration.

Operator: Thank you. If you would like to ask a question, please press the star or asterisk key, followed by the digit one. We will pause for a moment to allow everyone to signal. We have our first question from Aftab Awan from Sherman Securities. Please go ahead.

Aftab Awan: Okay, good evening everyone. My first question is regarding the Company's Financial Results, where devaluation of Pak rupees and increasing trend of oil prices was dominant. OGDCL's production has declined in first half. I would like to ask that how are you planning to arrest the decline in production? Further, can you state categorically how much gas and oil will be added to the production in next couple of years?

Zahid Mir: Thank you very much. First of all, looking at production volumes you may think that the production has declined, but, in fact it has not. Look at the total BOE numbers of the first Half Year 2017-18, which comes to 19 MMBOEs and now in this half year, the total is 19.40 MMBOE, which shows a slight increase in the total BOE numbers. You can see some reduction in gas production, which is obviously due to natural decline whereas significant enhancement in LPG production is witnessed. The main reason behind less oil production was due to the furnace oil crisis in November to December 2018 where the refineries, across the country, were not lifting oil due to the furnace oil high inventories. As a result, of this crisis, our production was curtailed from KPD/TAY and Nashpa fields. Similarly, reduction in the gas production was mainly due to the extended ATA at the Uch power plant by M/S UPL. I am pleased to inform you that currently these factors have been resolved and hopefully will not be repeated.

Now coming to your second part of the question on the quantum of gas or oil that we are expecting. Our projects in the pipeline are Dhok Hussain, Bitrisim, Mela, Thal West, Thal East, Jhal Magsi and Khewari. And if you total all these you will see that it's about 150 MMscfd gas in the next two to three years. We expect to not only offset the natural depletion but also to have some increase in net production of gas in the next two years or so.

Aftan Awan: Okay. My next question pertains to projects, historically, we have observed that usually execution of projects takes longer than expected. You have provided timeline for new projects do you expect that these will be adhered to?

Zahid Mir: Yes, there's a history, and I'm talking about 2006, 2008 and 2012, when the KPD project and Sinjhoro projects got delayed. But in the last four years, you would have seen that Nashpa project was awarded at the end of 2015, the contractor was mobilised in 2016 and it was completed without any delay. Now the Dhok Hussain project where 97% work has also been done and we are ready to supply the gas to SNGPL. SNGPL is planning to lay the pipeline and they have told us that pipeline should be completed in a month or two. Dhok Hussain Project deadline line is June 2019 but we can see production coming as early as end of April or May 2019.

Aftan Awan: Thanks Sir, my other question is towards the exploration efforts in Balochistan province due to better security situation, E&P companies might be doing more exploration in Balochistan. So, is there any project or any exploration well or any block that you are working on in Balochistan?

Zahid Mir: There are many blocks where we are working in Balochistan province. In fact, we have currently three seismic parties acquiring seismic data in Balochistan province and in the last two years, we have done extensive seismic surveys in the province. In the last three years, first time in the history of Pakistan, OGDCL has done record making exploration activities in the Balochistan province. Currently, we are drilling Zin Deep-2 well in Zin Block in Balochistan. We are also working in Block 28, and Kohlu block. There has been good progress where our partner MPCL is working in Block 28. By mid this year, we would be starting seismic activity in the area and then in the second half of this year, we'll also be starting the seismic activities in Kohlu block which has been in Force Majeure for the last many years.

Aftan Awan: Okay Sir, my next question is regarding offshore well. Can you tell us something about it? As per my understanding, 70% of the drilling target has been achieved. So, when do you think this would be completed? And can you give us some estimate about the discovery size? What is your expectation?

Zahid Mir: You are right about the 70% drilling completion. It may take another three weeks if all goes as planned to complete the well, and only then we will know the results. As far as the size is concerned, we have already said in past, it is a high risk well. Actual size of the reserves we will be shared once the drilling is complete.

Aftan Awan: Okay, thanks Sir.

Operator: Thank you, I'll now go to our next question from Asim Khan from UBL Funds, please go ahead.

Asim Khan: Thank you for the presentation, Sir. I had just one question, that is regarding the stake sale of MPCL share. I just wanted to ask if my understanding is correct that OGDCL has the first right of refusal. So, has OGDCL exercised its right.

Zahid Mir: It is correct that OGDCL have got the first right of refusal. As per the shareholder agreement, a price at which the Government of Pakistan is willing to sell its share needs to be determined. We can only take a decision once the price has been decided by the Government of Pakistan and is intimated to OGDCL.

Asim Khan: All right. I was just looking at OGDCL's numbers. Your productions peaked in FY'14 at around 78.5 million barrels of oil equivalent for the entire year. And till FY19, your production has dropped to around about 70 million barrels of oil equivalent, that's about 10-12% decline. And during this timeframe of about four-and-a-half, five years, you have spent about 250 billion on CapEx, and seismic activities. So, even though you have spent about PKR 250 billion during this four, five years' period, OGDCL has not been able to arrest the decline in production. So, my question is that if you getting additional production comes from the sale of the MPCL stake of 20% interest estimated at about PKR 25 billion to PKR 30 billion would not that be a cheaper way of increasing production volumes. You can actually increase your production on a stake-adjusted basis back to these production levels which is about one-tenth the cost that you have spent over four or five years for arresting the decline. So, in effect, your production would actually increase to 78.5 million barrels of oil which is the peak that you touched back in 2014. So, at one-tenth of the cost, you will actually be able to increase your production back to that level on an immediate basis. Isn't this a very lucrative option considering that OGDCL has also very strong balance sheet at this point in time?

Zahid Mir: Thank you very much for the advice, but it has to be an economic decision. The Company will make a decision on whether to acquire or not purely based on the economic analysis on commercial terms.

Asim Khan: Right, just to add a comment – I think if you look at the industry estimate, people are projecting about 25% of cash flow yield from MPCL from next year onwards considering that MPCL will now get the full entitlement price.

Zahid Mir: Okay, thank you very much.

Operator: Thank you. Our next question comes from Ali Hussain from FIM Partners. Please go ahead.

Ali Hussain: Thank you very much for the call. The question I had is regarding circular debt. You know, if you read media reports, there was recently a Sukuk that has been issued – Islamic Sukuk worth Rupees 200 billion issued by Government of Pakistan to settle part of the circular debt. I just wanted to hear your view on the circular debt situation and how do you see the potential of reaping some benefits from the Sukuk.

Zahid Mir: Well, we are hoping to get some part of that back to OGDCL, but obviously, this is still not finalized. Now, there are two things, which has happened. First is that Government is lending Pak Rupees 200 million and paying a reasonable amount of this Pak Rupees 200 million to SNGPL. SNGPL will be paying off to PSO for the LNG payments and also to us. Number two is, we believe that the cash flow situation of SNGPL and SSGCL after the recent hike in the gas price have improved. So we are expecting that their ability to pay the full invoices has improved. We are hoping to see some improvement in the receivables from now onward.

Ali Hussain: Okay. I meant to ask what is the amount that is outstanding, currently, directly to OGDC?

Zahid Mir: The major chunk of our receivables are due mainly from Sui companies i.e, Sui Southern and Sui Northern which is about Pak Rupees 155 billion.

Ali Hussain: Okay. All right. Thank you very much.

Operator: Thank you. We will take our next question today from Muhammad Daniyal from EFG Hermes.

Muhammad Daniyal: As you mentioned that there are a lot of activities going on in Balochistan, but at the same time that a lot of blocks were relinquished in 2018 in Balochistan. And that too without even conducting seismic activity. So, what is your view on that? How do we perceive that?

Zahid Mir: We have not relinquished any blocks in Balochistan without conducting work program. There is, however, a possibility that we have relinquished a block without fulfilling the complete commitment. For example, after conducting seismic in a block if after the processing and interpretation, we reached to the conclusion that there is no evidence of a sub structure which can be drilled. So we transfer the remaining work program (drilling of a firm well) commitment for this block to some other block.

Muhammad Daniyal: My second question is, given the global scenario, how do you see the pricing of rigs and seismic surveys going forward? So, what is your view on that in the next year or two given the prices of oil?

Zahid Mir: Actually, what has happened over the last two years is that the services cost in Pakistan has come down. The cost of the rigs has come down from $25,000 per day to about $17,000 per day. Recently, the increase in the oil price has generated activity worldwide. And there has been some increase in the services cost outside Pakistan. We have not yet seen a significant increase as far as the services cost is concerned.

Muhammad Daniyal: All right. In November 2018, the Government of Pakistan offered some new blocks. Did OGDCL participated in the same. Has there been any update on new blocks?

Zahid Mir: There were ten blocks on offer and we submitted bids on five blocks, and out of five, we have acquired the rights to explores in three blocks as operated, and one as non-operated block.

Muhammad Daniyal: All right. Given that the specification of gas from different fields is very different from each other, but can you tell a generic ratio of how much LPG can be produced from, say, 1 MMcf of gas? I know this is a bit technical, but if you have some range of ratio for OGDCL.

Zahid Mir: The quantum of LPG extraction from gas depends upon the heavier hydrocarbons content in the gas. So it varies from field to field depending upon the gas specification of that particular field.

Muhammad Daniyal: All right. And just a follow-up question. You said that you have around $70 billion in investments, so is there any plan to utilise that Zin shallow gas by starting a power plant or anything? Or how do you plan to spend that $70 billion cash?

Zahid Mir: OGDCL is drilling a deep well in Zin D&PL. Zin upper is a low-pressure gas. We are drilling a horizontal well there to improve the deliverability of a single well, and we are drilling deeper to see if we can find more gas in the deeper horizon with a higher Btu content.

Muhammad Daniyal: All right. Thank you so much.

Operator: Thank you. Our next question comes from Ovais Hussain from HBL Asset Management.

Ovais Hussain: Thank you. I just have one question. In terms of the fact that you already mentioned the production decline was somehow related to the fact that the dispatches to refineries were down, do we have a sense of how the government or you guys or anyone in the chain is looking to cater to this problem moving ahead? Because otherwise, the decline in production will end up becoming a recurring phenomenon.

Zahid Mir: Yes, the government is quite serious in resolving this issue and I have attended a few meetings on the agenda. One of the options being looked into is to allow export of fuel oil which is being produced in Pakistan. Another way is to ban import of any fuel oil and try to utilise the power plants which are on fuel oil in Pakistan. Currently refineries in Pakistan are producing about 8,000 tonnes of fuel oil every day. So, either they will export this fuel oil or it will be utilized in the power plants.

Ovais Hussain: So, finally, one last thing. Our understanding is if you look at the newspapers, they are quoting a circular debt number, ranging from Pak Rupees 200 billion to somewhere around Pak Rupees 600 billion. What is your understanding in terms of it? Where is that number currently and what is the government looking to do with that?

Zahid Mir: The government is raising Pak Rupees 200 billion to settle a portion of circular debt to some extent.

Operator: Last question comes from Bilal Arshad from Maple Leaf Capital Limited. Please go ahead.

Bilal Arshad: I just wanted to ask that despite the dollar depreciation of about 32% year-on-year, and despite doing more seismic work during this quarter, I was just looking at it that although OGDCL had drilled fewer wells during these past six months compared to last year, but the seismic survey, they have done more over the larger area. But despite all that, the exploration expense has come down significantly, about 50% compared to previous levels. So, what would be the reason for that?

Irteza Ali Qureshi: Basically the reason is the reduction in the cost of dry holes. This year, we had a cost of Rs 1.6 billion as the dry hole cost, as opposed to Rs 4 billion in the previous year. We have booked Wasan-1 as a dry hole this year, versus Pirkoh Deep-1, Ranipur and Qadirwali-1 in the previous year. There were three wells that were booked as dry holes last year as against one this year.

Bilal Arshad: Okay. OGDCL had total Capex on the exploration and development activity at around PKR 42 billion of which around PKR 24 billion was earmarked for exploration and exploration wells. Is that still on track because out of the target of 22 wells, so far only six have been drilled?

Zahid Mir: We are quite confident to achieve a target of 21 wells during the current FY2019. Furthermore, OGDCL has spud 3 more wells in January & February 2019; so, nine wells have been spud so far. Also three rigs are under shifting for the new location, so in the next month, you will see another three being spud. We have planned to spud 21 wells and we'll be able to achieve this target.

Bilal Arshad: Okay. So just one last question. Out of this PKR 30 billion revised Capex guidance, how much would you allocate to the development projects and how much to the exploration and development wells?

Zahid Mir: Well, majority of course will be spent on the wells.

Bilal Arshad: Okay. Thank you, Sir.

Operator: There are no further questions in the queue at this time. I would like to turn the conference back to our speakers for any additional or closing remarks.

Mr. Zahid Mir: Thank you very much everybody. We are very grateful for your participation. I hope to see you again in six months' time. Please note that our Investor Relations team is available to attend any further queries that you may have. Have a good evening, and goodbye.